

128 FERC ¶ 61,229
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Jon Wellinghoff, Chairman;
Sudeen G. Kelly, Marc Spitzer,
and Philip D. Moeller.

Midwest Independent Transmission
System Operator, Inc.

Docket No. ER09-1435-000

ORDER CONDITIONALLY ACCEPTING PROPOSED TARIFF REVISIONS

(Issued September 8, 2009)

1. On July 10, 2009, under section 205 of the Federal Power Act (FPA),¹ Midwest Independent Transmission System Operator, Inc. (Midwest ISO) submitted a new Schedule 34 (Allocation of Costs Associated with Reliability Penalty Assessments) and revisions to section 7 (Billing and Payment, Defaults and Remedies) to its Open Access Transmission, Energy and Operating Reserve Markets Tariff (Tariff). Midwest ISO states that the proposed revisions would allow Midwest ISO to seek Commission approval for recovery of certain penalties that may be assessed against Midwest ISO by the Commission, the North American Electric Reliability Corporation (NERC), or a Regional Entity for violations concerning Reliability Standards as well as other regulatory requirements.² As discussed below, we conditionally accept the proposed tariff revisions, effective September 9, 2009, as requested, subject to a compliance filing, as discussed below.

I. Background

2. Section 1211 of the Energy Policy Act of 2005 (EPAct 2005)³ added section 215 to the FPA, which provides for the development and enforcement of mandatory reliability

¹ 16 U.S.C. § 824d (2006).

² Currently, eight Regional Entities with enforcement authority share NERC's mission for their respective geographies within North America.
(<http://www.nerc.com/page.php?cid=19|119>)

³ 16 U.S.C. § 824o (2006).

standards by an electric reliability organization (ERO) to be certified by the Commission. The ERO and Regional Entities may impose penalties for violations of reliability standards, subject to Commission approval.⁴ On July 20, 2006, the Commission certified NERC as the ERO.⁵

3. Order Nos. 672 and 672-A⁶ implemented the requirements of EPAct 2005 regarding the selection, standard-setting procedures, and operational aspects of the ERO. In these orders, the Commission denied requests to (1) exempt non-profit regional transmission operators (RTO) and independent system operators (ISO) from monetary penalties for violations of the reliability standards, or (2) authorize RTOs and ISOs to recover such monetary penalties from their customers on an automatic basis. Rather, the Commission stated that it would consider proposals to recover the costs of any such penalties imposed on RTOs and ISOs under section 205 of the FPA on a case-by-case basis.⁷

4. Each NERC-developed, Commission-approved reliability standard includes an “applicability” section that identifies the types of Registered Entities that must comply with the standard.⁸ The categories of applicable entities were developed using the NERC functional model, and include generator owners, transmission owners, transmission operators, or reliability coordinators. All RTOs and ISOs have registered as transmission service providers under the NERC functional model, and have registered for other functions as appropriate. Thus, an RTO or ISO that fails to comply with the requirements of the applicable Reliability Standards may be assessed a penalty by a Regional Entity, the ERO, or the Commission pursuant to section 215(e) of the FPA. Each Regional

⁴ The Commission, on its own motion, may also investigate violations of the reliability standards and impose penalties. 16 U.S.C. § 824o(e)(3) (2006).

⁵ *North American Electric Reliability Corp.*, 116 FERC ¶ 61,062, *order on reh’g*, 117 FERC ¶ 61,126 (2006).

⁶ *Rules Concerning Certification of the Electric Reliability Organization; and Procedures for the Establishment, Approval and Enforcement of Electric Reliability Standards*, Order No. 672, FERC Stats. & Regs. ¶ 31,204, at P 634-35, *order on reh’g*, Order No. 672-A, FERC Stats. & Regs. ¶ 31,212 (2006).

⁷ Order No. 672, FERC Stats. & Regs. ¶ 31,204 at P 634-35; Order No. 672-A FERC Stats & Regs. ¶ 31,212 at P 55-58.

⁸ The specific characteristics that determine whether a user, owner or operator of the Bulk-Power System is registered for a particular function and thus must comply with applicable standards are set forth in the NERC Statement of Registry Criteria.

Entity has a Compliance Monitoring and Enforcement Program with which to monitor, assess, and enforce compliance with reliability standards. Each Regional Entity's program is based on NERC's *pro forma* Compliance Monitoring and Enforcement Program, and is set out in Exhibit D of the Regional Entity's delegation agreement with NERC.⁹

5. In Order No. 693, the Commission stated that it is important to have as much certainty and stability as possible regarding which users, owners, and operators of the bulk power system must comply with which reliability standards. NERC, as the ERO, has developed its compliance registry process to accomplish this goal. The Commission noted that it has held that NERC's compliance registry process is a reasonable means "to ensure that the proper entities are registered and that each knows which Commission-approved reliability standard(s) are applicable to it."¹⁰ The Commission stated that it will not assess penalties against an entity that has not previously been put on notice, through the NERC registration process, that it must comply with particular reliability standards.¹¹ Under this process, if NERC later discovers that an unregistered entity should have been subject to a reliability standard, NERC may add the entity, and possibly other entities of a similar class, to the registration list and direct future corrective action.¹² The Commission stated that it believes that this process should prevent an entity from being subject to a penalty for violating a reliability standard without prior notice that it must comply with that reliability standard.

6. On April 2, 2007, in Docket Nos. ER07-701-000 and AD07-12-000, Midwest ISO proposed to amend its Open Access Transmission and Energy Markets Tariff to add Schedule 10-ERO in an effort to provide for the recovery of penalties that are imposed on Midwest ISO by the Commission, the ERO, or by a Regional Entity for violations of mandatory Reliability Standards. The Commission rejected Midwest ISO's proposal without prejudice and established a staff technical conference to address generically the

⁹ See, e.g., *North American Electric Reliability Council*, 119 FERC ¶ 61,060, at P 25 (2007), *order on reh'g*, 122 FERC ¶ 61,245 (2008).

¹⁰ *Mandatory Reliability Standards for the Bulk Power System*, Order No. 693, FERC Stats. & Regs. ¶ 31,242, at P 92 (quoting *North American Electric Reliability Corp.*, 116 FERC ¶ 61,062, at P 689 (2006)), *order on reh'g*, Order No. 693-A, 120 FERC ¶ 61,053 (2007).

¹¹ Order No. 693, FERC Stats. & Regs. ¶ 31,242 at P 97.

¹² See NERC Rules of Procedure, § 500.

issues raised by the proposal concerning Reliability Standard compliance and enforcement in regions with non-profit RTOs and ISOs.¹³

7. As a result of the technical conference, the Commission issued a Guidance Order¹⁴ outlining how RTOs and ISOs seeking to recover costs they incur for reliability penalties assessed under section 215 of the FPA could provide notice of such potential recovery in their tariffs or contracts. In the Guidance Order, the Commission acknowledged the careful balance required when addressing recovery of reliability penalties by RTOs and ISOs. The Commission noted that, as the facilitators and managers of the nation's largest and most complex energy markets, RTOs and ISOs are essential to maintaining the reliability of the electric system. However, the Commission also noted that, because these entities are typically member-supported non-profit organizations, they do not have an independent source of funds with which to pay monetary penalties assessed to them for violation of Reliability Standards. The Commission stated that granting blanket authority to pass through monetary penalties to their customers automatically, however, could significantly reduce the incentives for RTOs and ISOs to maintain strict compliance with reliability standards. As a result, the Commission concluded that it would only accept penalty recovery mechanisms under which the Commission could review the appropriateness of each penalty on a case-by-case basis in filings under section 205 of the FPA.

8. The Commission has previously accepted tariff proposals for recovery of monetary penalties for Reliability Standard violations from PJM Interconnection, L.L.C., Southwest Power Pool, Inc., and New York Independent System Operator, Inc.¹⁵

II. Midwest ISO's Proposal

9. Midwest ISO states that the purpose of the proposed Schedule 34 is to add a new mechanism to its Tariff in order to recoup the costs it incurs for penalties assessed by the Commission, NERC and/or Regional Entity for violations of NERC Reliability Standards. Midwest ISO asserts that its proposal is just and reasonable and fully

¹³ *Midwest Independent Transmission System Operator, Inc.*, 119 FERC ¶ 61,222 (2007).

¹⁴ *Reliability Standard Compliance and Enforcement in Regions with Regional Transmission Organizations or Independent System Operators*, 122 FERC ¶ 61,247 (2008) (Guidance Order).

¹⁵ *See PJM Interconnection, L.L.C.*, 124 FERC ¶ 61,260 (2008), *Southwest Power Pool, Inc.*, 126 FERC ¶ 61,061 (2009) and *New York Independent System Operator, Inc.*, 127 FERC ¶ 61,196 (2009).

complies with the Commission's Guidance Order. Midwest ISO states that, as the Guidance Order acknowledges, ISOs are non-profit entities that have no reserves to pay penalties assessed against them and, like similarly situated ISOs and RTOs, Midwest ISO's current cost recovery mechanisms are designed to recover the costs associated with the specific services Midwest ISO provides and not Reliability Standards penalties. Midwest ISO states that there are no current means for it to collect revenues to pay penalty costs it may be assessed for its own violations or because of its role as a Registered Entity, even if violations are caused by another entity.

10. The proposed tariff amendments would authorize Midwest ISO to make a section 205 filing to seek Commission approval to recover on a case-by-case basis such penalty costs in two ways: (1) if NERC or the Regional Entity finds that a Midwest ISO Tariff Customer or Member that is subject to Compliance Monitoring and Enforcement Program in the United States is at fault, Midwest ISO may seek under section 205 for a direct assignment of the costs to that Tariff Customer or Member; and (2) if Midwest ISO cannot directly assign the costs to a Tariff Customer or Member at fault or if Midwest ISO itself is at fault, Midwest ISO may seek under section 205 to recover those penalty costs on a system-wide basis, as explained in more detail below.

A. Direct Assignment

11. The first method of recovery Midwest ISO proposes is for reliability penalties assigned to Midwest ISO due to the action or inaction of a Tariff Customer(s) or Member(s). In this section, Midwest ISO proposes to seek Commission approval in a section 205 filing to directly assign and bill those penalty costs to the offending Tariff Customer(s) or Member(s), after providing the entity/ies with reasonable prior written notice and the opportunity to participate in the underlying Compliance Monitoring and Enforcement Program or "root cause" proceeding.¹⁶

12. Section 2 of Schedule 34 provides that Midwest ISO will notify NERC, the Regional Entity, and the Commission of its allegations that a Tariff Customer(s) or Member(s) may have contributed to the alleged violation and that Midwest ISO intends to hold the Tariff Customer(s) or Member(s) responsible for a portion of or all the monetary penalties that result from the investigation. In addition, section 2 provides that if, as a result of a proceeding under a Compliance Monitoring and Enforcement Program investigation, it is determined that a Tariff Customer(s) or Member(s) was identified as a

¹⁶ Schedule 34 - Original Sheet No. 2280U. A "root cause" proceeding is an investigation into the "root cause" of the reliability violation conducted by NERC or its Regional Entity, pursuant to the Compliance Monitoring and Enforcement Program approved by the Commission. *See North American Electric Reliability Council*, 119 FERC ¶ 61,060 (2007); *order on reh'g*, 122 FERC ¶ 61,245 (2008).

contributor(s) to or the root cause of the violation, Midwest ISO will hold the Tariff Customer(s) or Member(s) responsible for all or a portion of the monetary penalty by making a section 205 filing with the Commission.

13. Furthermore, section 2 provides that if a Tariff Customer(s) or Member(s) fails to participate in the Compliance Monitoring and Enforcement Program proceedings it will not prevent Midwest ISO from assigning the costs associated with the penalty to the responsible Tariff Customer(s) or Member(s), provided all other conditions set forth in section 2 have been satisfied.

B. System-Wide Penalty

14. The second method of recovery of reliability penalties in Midwest ISO's proposal, system-wide allocation, applies to penalties Midwest ISO incurs for reliability violations that cannot be directly assigned to a particular, identifiable Tariff Customer or Member, or are the fault of Midwest ISO itself. Section 3 of Schedule 34 authorizes Midwest ISO to seek Commission approval pursuant to section 205 to recover these penalty costs on a case-by-case basis by spreading the costs among all Tariff Customers and Members.

15. Section 3 provides that Midwest ISO will notify in writing all of its Tariff Customers or Members of a confirmed violation as soon as possible after notification by the Commission of its confirmation of a penalty assessment against Midwest ISO that cannot be assigned under section 2 of Schedule 34.

16. Section 3 also provides that Midwest ISO will assess all Tariff Customers and Members a portion of the monetary penalty utilizing a Commission-accepted methodology to allocate a portion of or all the costs of the monetary penalty among all Tariff Customers and Members. Furthermore, Midwest ISO will bill its Tariff Customers and Members in the next monthly invoice following a Commission order accepting the methodology. Midwest ISO may recover penalty charges over several months if, in its discretion, Midwest ISO determines such method of recovery to be a prudent course of action. Section 3 also provides that, if one or more entities who otherwise would have been apportioned a portion of the penalty cost are no longer Tariff Customers or Members of Midwest ISO, their portion shall be assigned to the rest of the remaining Tariff Customers and Members on a proportional basis in order to fully recover the penalty amount as authorized by the Commission.

C. Section 7 – Default Procedures for Tariff Customers and Members in the Event of a Penalty

17. In addition, Midwest ISO proposes revisions to section 7 (Billing and Payment, Defaults and Remedies) of Module A of its Tariff. Midwest ISO proposes new section 7.24, which notifies Tariff Customers and Members that, once a Commission order has been issued in regards to a reliability standard penalty amount, Midwest ISO shall invoice

such amounts in accordance with the terms of Schedule 34 and the applicable Commission order. If a Tariff Customer or Member fails to make the required payment, then the provisions in section 7.16 (Default) and any applicable subsections of section 7 shall apply to a Tariff Customer or Member for such non-payment.

D. Other Tariff Changes

18. Midwest ISO also submits revised tariff sheets to reflect corrections to the Table of Contents from previously filed tariff sheets in other proceedings that were not updated at the time such tariff sheets were submitted. Additionally, Midwest ISO updated the entry for Schedule 33 in the Table of Contents to ensure the correct reference.

III. Notice of Filing and Responsive Pleadings

19. Notice of Midwest ISO's July 14, 2009 filing was published in the *Federal Register*, 74 Fed. Reg. 36,187 (2009), with interventions or protests due on or before July 31, 2009.

20. Detroit Edison Company, Hoosier Energy Rural Electric Cooperative, Inc., Southern Illinois Power Cooperative, Wisconsin Electric Power Company, Constellation Energy Commodities Group, Inc., Constellation NewEnergy, Inc., and Exelon Corporation filed timely motions to intervene. The Illinois Commerce Commission (Illinois Commission) filed a notice of intervention. The Midwest ISO Transmission Owners (Midwest ISO TOs) and American Transmission Company LLC (ATC) filed timely motions to intervene and protests. American Municipal Power, Inc. (AMP) and Consumers Energy Company (Consumers Energy) filed timely motions to intervene and comments. The Organization of MISO States (OMS) filed comments. Midwest ISO filed an answer to the protests. International Transmission Company, Michigan Electric Transmission Company, LLC, and ITC Midwest LLC (collectively, ITC) filed an answer to Midwest ISO's answer.

A. Protests and Comments

21. ATC argues that the proposed Schedule 34 does not afford basic due process rights. Specifically, ATC argues that Schedule 34 is missing the express recognition that if a party is not afforded the opportunity to participate "fully" in the Regional Entity or NERC proceedings, then no penalty can or should be assessed against that party. Additionally, ATC recommends revisions to Schedule 34 that address Tariff Customers' or Members' participation in the Compliance Monitoring and Enforcement Program proceedings.

22. OMS argues that section 3 of Schedule 34 should be revised to incorporate a notification process and allow affected Tariff Customers and/or Members to participate in the penalty decision process in cases where a penalty cannot be directly assigned and will

be shared among Tariff Customers and/or Members. Consumers Energy also argues that in either situation (direct assignment or system-wide sharing) Midwest ISO should be required to give notice to potentially affected Tariff Customers and/or Members as soon as possible after notifications by NERC or the Regional Entity of the commencement of the investigation.¹⁷

23. OMS also argues that Schedule 34 should be revised to exempt from the shared penalty charge Tariff Customers and Members that were not Tariff Customers or Members of Midwest ISO at the time of the event that led to the penalty. Likewise, OMS argues that Midwest ISO's proposal to reallocate penalty assessments from Tariff Customers or Members that were Tariff Customers or Members when the event leading to the penalty occurred, but which subsequently ceased to be Midwest ISO Tariff Customers or Members, is discriminatory to the remaining Tariff Customers and/or Members. AMP also argues that the Commission should direct Midwest ISO to modify its Tariff to require Midwest ISO to take all reasonable steps to impose responsibility on, and collect appropriate penalty amounts from, former Tariff Customers and Members, and such collections should be credited to reduce any amounts paid by current Tariff Customers and/or Members.

24. The Illinois Commission states that it is a member of OMS, but for procedural reasons, abstained from voting on the comments at the OMS Board meeting. Since the OMS Board meeting, the Illinois Commission has had an opportunity to consider the comments and indicates that it supports the comments submitted by OMS.

25. AMP states that it has no disagreement with the notice sections of Midwest ISO's proposed tariff additions. However, AMP requests that the Commission assure participants in this docket that the standards set forth in the Commission's Guidance Order will govern application of the Tariff. Specifically, AMP points to the Guidance Order at P 23 and P 24 where the Commission notes that due process requires that a targeted entity be notified early in any investigation, inquiry or hearing that it may be deemed responsible for a violation and that the Commission will not allow the direct assignment of penalty costs by an RTO or ISO to another entity under section 205 unless that entity had previously been put on notice of its potential liability. In light of this guidance, AMP argues that section 2 of the proposed Schedule 34 does not tackle the circumstances in which, during the course of the investigation, it becomes apparent that one or more Tariff Customers or Members, not originally named and notified, might have contributed to the Reliability Standard violation and may be responsible for all or part of the penalty.¹⁸ AMP argues that, when a new potentially responsible entity is identified, a

¹⁷ Consumers Energy, July 31, 2009 Comments at 4.

¹⁸ AMP, July 30, 2009 Comments at 4.

new inquiry must commence after the new entity is given notice. Further, AMP argues that the Commission must not be free to assign some or all of a penalty cost to a Member or Tariff Customer named for the first time in the course of a section 205 proceeding where the entity was previously without notice that it was implicated. AMP argues that the Commission should make clear, as a general statement or by requiring a modification to the Tariff, that any finding during the course of a section 205 proceeding that an entity other than one named by the RTO or ISO at the commencement of the section 205 proceeding is responsible for any portion of a penalty payment will lead to a new proceeding and not to imposition of responsibility on an entity without previous notice.

26. Midwest ISO TOs do not oppose Midwest ISO's proposal, but propose certain modifications that they state are required to provide greater clarity and consistency. First, and in accordance with arguments made by OMS and AMP, Midwest ISO TOs state that the proposed Schedule 34 should be modified to provide a continuing obligation for Tariff Customers and Members to pay costs allocated to them under Schedule 34 in the event that they cease to be a Tariff Customer or Member.¹⁹ Midwest ISO TOs state that under the Midwest ISO Transmission Owners Agreement, "financial obligations incurred and payments applicable to time periods prior to the effective date of such withdrawal shall be honored by the Midwest ISO and the withdrawing Owner."²⁰ Moreover, Midwest ISO TOs point out that Members²¹ "who withdraw from the Midwest ISO continue to be responsible for costs incurred prior to their withdrawal such as financial obligations under the Midwest ISO Regionally Beneficial Project Criteria ("RECB") cost allocation method for Network Upgrades."²²

27. Second, Midwest ISO TOs recommend revising two sentences in section 3 of Schedule 34 on Original Sheet No. 2280W as follows:

A portion of or all such penalty costs may be allocated among all Tariff Customers and/or Members where the Transmission Provider itself is responsible for a confirmed violation of a Reliability Standard or where the Transmission Provider is assessed a penalty because of its status as a

¹⁹ Midwest ISO TOs, July 31, 2009 Protest at 3.

²⁰ *Id.* at 4.

²¹ Midwest ISO TOs' July 31, 2009 Protest at page 4 refers to "Tariff Customers" withdrawing from the Midwest ISO, but their cite to the Tariff at Attachment FF § III.A.2.i, Original Sheet No. 3480 (Cost Responsibility for MTEP Projects) makes clear that Midwest ISO TOs' intent was to refer to "Members."

²² Midwest ISO TOs, July 31, 2009 Protest at 4.

*Registered Entity for a given Reliability Standard and the entity responsible for the violation cannot be assessed a penalty **by NERC, a Regional Entity, or the Commission** because of its status.*

*If there is an assessment of a monetary penalty against the Transmission Provider as the Registered Entity for a confirmed violation of a NERC Reliability Standard(s), either: (1) as a result of the Transmission Provider's own conduct or omission; or (2) as a result of a violation by another entity for whom the Transmission Provider is the Registered Entity where the entity is not on the NERC Compliance Registry and therefore cannot be directly assessed a penalty **by NERC, a Regional Entity, or the Commission** because of its status....^[23]*

28. Third, Midwest ISO TOs argue that section 2 of Schedule 34 is ambiguous and could be read as providing Midwest ISO with discretion to apportion fault for violations of reliability standards, which contravenes the Commission's guidance that it should be NERC, the Regional Entity, or the Commission, and not the RTO, that determines responsibility for violations of reliability standards.²⁴ Accordingly, Midwest ISO TOs recommend revising two sentences in Original Sheet No. 2280V as follows:

*If, as a result of proceedings under the [Compliance Monitoring and Enforcement Program], it is determined **by the [Compliance Monitoring and Enforcement Program] process** that the Tariff Customer(s) or Member(s) identified by the Transmission Provider ~~as~~**are** contributor(s) to or the "root cause(s)" of the confirmed violation, the Transmission Provider will hold the Tariff Customer(s) or Member(s) responsible for ~~a~~**that** portion of or all of the monetary penalty assessed as a result of the confirmed violation **directly attributable to the Tariff Customer(s) or Member(s)** by making a filing with the Commission under section 205 of the Federal Power act to assign a portion of or all of the costs of the monetary penalty directly to the Tariff Customer(s) or Member(s);*

*A failure by a Tariff Customer(s) or Member(s) to participate in the [Compliance Monitoring and Enforcement Program] proceedings, **after***

²³ *Id.* at 5.

²⁴ *Id.* at 6, citing Guidance Order, 122 FERC ¶ 61,247 at P 22-23.

***notice and an opportunity to participate has been provided**, will not prevent the Transmission Provider from directly assigning the costs associated with a monetary penalty to the responsible Tariff Customer(s) or Member(s) provided all other conditions set forth herein have been satisfied.*

B. Answers

29. Midwest ISO rejects AMP's assertion that Midwest ISO should be required to commence a new inquiry whenever a new, potentially responsible entity or entities is identified in the course of a Compliance Monitoring and Enforcement Program investigation. Midwest ISO argues that this would be inconsistent with the Guidance Order, which provides that it would be unnecessary and duplicative for RTOs and ISOs to conduct their own inquiries to assess responsibilities for violations of the Reliability Standards. Rather, Midwest ISO argues that insufficient notice is a due process argument that is more appropriately considered on a case-by-case basis in a section 205 proceeding based on the facts of a particular penalty assessment. Likewise, in response to OMS' and Consumers Energy's arguments about providing notice in a shared penalty situation, Midwest ISO states that it will provide the appropriate notice in the appropriate manner as each situation dictates, and that an entity that does not agree that proper notice was provided can make such objections in the context of a section 205 filing based on the facts of a particular penalty assessment.

30. With respect to arguments raised by AMP, OMS and Midwest ISO TOs in regard to the recovery of penalties from former Tariff Customers or Members of Midwest ISO and protection of current Tariff Customers or Members from imposition of past penalties, Midwest ISO states that it will vigorously pursue such appropriate entities for the collection of their portion of penalty costs pursuant to the applicable terms of the then-current Tariff. Midwest ISO notes, however, that it may take years for penalties to be assessed and approved by the Commission, and therefore Midwest ISO may not be able to collect such amounts from former Tariff Customers or Members who were Tariff Customers or Members at the time of the events that led to the assessment of the penalties. In such cases, Midwest ISO seeks to treat uncollectible penalty costs as it would other bad debt and recover them from the then-current Tariff Customers and Members.

31. Midwest ISO also responds to Midwest ISO TOs' requests for clarifying changes to the Tariff. With respect to Midwest ISO TOs' request that the Tariff read that "a portion of or all of such penalty costs may be allocated among all Tariff Customers and or Members where the Transmission Provider itself is responsible for a confirmed violation..." Midwest ISO asserts that the language was specifically selected because, if a penalty could not be directly assigned, Midwest ISO would need to uplift those penalty costs to all possible entities, including Tariff Customers *and* Members. With respect to Midwest ISO TOs' request to insert "NERC, a Regional Entity, or the Commission" in section 3, Midwest ISO agrees that those groups are the most likely entities to assess

penalties against the Midwest ISO. However, Midwest ISO proposes to leave specific name references out of Schedule 34 in an effort to avoid the need for future filings should the names or references to those entities change. Midwest ISO further states that it will amend the language if so directed by the Commission.²⁵ Finally, Midwest ISO disagrees with Midwest ISO TOs' concern that section 2 of Schedule 34 could be read as providing the Midwest ISO with the discretion to apportion fault for violations. Midwest ISO states that the Guidance Order²⁶ makes clear that NERC, the Regional Entity or the Commission will be responsible for conducting the investigations and hearings that may potentially lead to an assessment of penalties. Midwest ISO argues that section 2 only provides for notice to an entity of it being potentially affected by an alleged violation, not Midwest ISO's assumption of discretion to apportion fault. In any event, Midwest ISO argues that such objections are more appropriately considered on a case-by-case basis in a section 205 proceeding.

32. ITC responds to Midwest ISO's statement in its answer that the language in section 3 of Schedule 34 to allocate unassigned penalty costs – among all Tariff Customers *and* Members – was specifically drafted to ensure that Midwest ISO could uplift penalty costs to all possible entities. ITC argues that the language Midwest ISO proposes would foreclose a case-by-case analysis by the Commission in a section 205 filing. Thus, ITC requests that the Commission adopt the clarifying change proposed by the Midwest ISO TOs to section 3 of Schedule 34.

IV. Discussion

A. Procedural Matters

33. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2009), the notice of intervention and timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding.

34. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2009), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept Midwest ISO's answer and ITC's answer because they have provided information that assisted us in our decision-making process.

²⁵ Midwest ISO, August 18, 2009 Answer at 9.

²⁶ *Id.* at 10, citing Guidance Order, 122 FERC ¶ 61,247 at P 22.

B. Substantive Matters

35. We will conditionally accept Midwest ISO's proposed revisions to its Tariff to become effective September 9, 2009, as requested, subject to a compliance filing, as discussed below. With the changes discussed below, we find that Schedule 34 provides a reasonable mechanism for Midwest ISO to seek recovery of the costs of a monetary penalty assessed against Midwest ISO for a Reliability Standard violation, either on a direct-assignment basis or to be allocated broadly to all Tariff Customers and Members. Schedule 34 also serves to notify Tariff Customers and Members of their potential responsibility for costs of monetary reliability penalties assessed to Midwest ISO. Therefore, Schedule 34 meets the notice requirement set out in the Guidance Order.²⁷

36. Also in accordance with the Guidance Order, Schedule 34 does not provide for automatic pass-through of costs or for a *de novo* investigation by Midwest ISO as an RTO. Rather, under Schedule 34, Midwest ISO may only directly pass through the costs of a penalty when a Regional Entity, NERC, or the Commission concludes from its fact-finding that the targeted entity directly contributed to or is found to have been a "root cause(s)" of the violation. Schedule 34 also requires the Commission's approval, through a section 205 filing, of pass-through of the costs of each specific penalty.

37. With respect to the concerns that a notification process should be incorporated into section 3 of the proposed Schedule 34, in cases where the penalty cannot be directly assigned and will be shared among all Tariff Customers and Members, we find that such a notification process is not needed. As stated above, Schedule 34 serves to notify all Tariff Customers and Members of their potential responsibility for the costs of monetary reliability penalties assessed to Midwest ISO. Further, prior to any applicable penalty being shared among the Tariff Customers and/or Members, Midwest ISO is required to make a section 205 filing with the Commission. That proceeding will provide all affected parties notice of the potential penalty cost allocation arrangements, and allow all

²⁷ The Guidance Order states:

[W]e will not allow the direct assignment of penalty costs to another entity under section 205 unless that entity had previously been put on notice of its potential liability for penalty costs in the event that it contributed to the RTO or ISO's violation of a Reliability Standard and incurrance of the penalty. It is therefore important for the RTOs and ISOs to include provisions regarding the appropriate responsibility for reliability-related monetary penalties in their contracts with their members and customers and/or in their Tariffs

Guidance Order, 122 FERC ¶ 61,247 at P 24.

affected parties the opportunity to intervene and comment on any such potential penalty cost allocation arrangements. Additionally, as the Commission has stated in previous orders, we will consider interventions and participation by third parties in Compliance Monitoring and Enforcement Program proceedings, as necessary, on a case-by-case basis.²⁸ Finally, to clarify that Midwest ISO must provide notification to its Tariff Customers *and* Members pursuant to section 3 of Schedule 34, not Tariff Customers *or* Members, we direct Midwest ISO to revise the second sentence on Original Sheet No. 2280W to change “or” to “and” so that the sentence reads as follows:

*The Transmission Provider shall notify, in writing, all of its Tariff Customer(s) **and** Member(s) of a confirmed violation as soon as possible after notifications by FERC or FERC’s confirmation of a penalty assessment against the Transmission Provider that cannot be directly assigned under Section 2 of this Schedule.*

38. With respect to concerns raised by AMP that proper notice and opportunity be afforded in cases where a new entity is found potentially responsible for a violation of a Reliability Standard later in the investigation and penalty cost assignment process, we reiterate the statement in the Guidance Order that the Commission will not entertain a section 205 filing unless the targeted entity has been notified during the course of the investigation, other inquiry into, or hearing of that matter, that an RTO or ISO believes that the targeted entity may be responsible for a violation.²⁹ Further, we emphasize that in Order No. 672, the Commission took steps to ensure that the investigation and hearing process to be employed by NERC and the Regional Entities will be thorough and accurate and will comport with the requirements of due process.³⁰ In addition to the due process protections described above in Order No. 672 and the Guidance Order, and in light of the nascent stage of the enforcement scheme involving Reliability Standards, the Commission will review due process concerns on a case-by-case basis.

39. With respect to ATC’s and Midwest ISO TOs’ concerns that the proposed tariff language needs to be changed to clarify that no penalty should be directly assigned unless that entity is afforded the right to participate in the Compliance Monitoring and Enforcement Program process, we agree in part. As a general matter, Schedule 34, as

²⁸ See *North American Electric Reliability Council*, 122 FERC ¶ 61,245, at P 84 (2008); see also *North American Electric Reliability Council*, 119 FERC ¶ 61,060, at P 150 (2007).

²⁹ Guidance Order, 122 FERC ¶ 61,247 at P 23.

³⁰ *Id.* P 22, citing Order No. 672, FERC Stats & Regs. ¶ 61,204 at P 450-638.

proposed, provides that, as a condition to being directly assigned a penalty, the Tariff Customer(s) or Member(s) is/are provided the opportunity to participate in all relevant processes under the Compliance Monitoring and Enforcement Program.³¹ However, we find that Midwest ISO TOs' proposed changes to section 2 of Schedule 34 clarify that the Compliance Monitoring and Enforcement Program process is the process by which individual Tariff Customers and/or Members will be found responsible for penalties, and that only that portion of a penalty for which a Tariff Customer or Member is found responsible may be assigned. We also find Midwest ISO TOs' proposed changes to section 2 of Schedule 34 will clarify that an entity must have been given notice and an opportunity to participate in the Compliance Monitoring and Enforcement Program proceedings in order for the entity's failure to participate to not act as a bar to direct assignment of penalties. With these clarifying changes to section 2 of the proposed Schedule 34, we find that Midwest ISO's proposed language will satisfy ATC and Midwest ISO TOs' concerns about participation in the Compliance Monitoring and Enforcement Program process.

40. AMP, OMS and Midwest ISO TOs argue that penalties must be recovered against culpable former Tariff Customers and/or Members, and raise concerns about recovering penalty costs from current Tariff Customers and/or Members who were not a part of Midwest ISO during the events giving rise to the penalty. Midwest ISO responds that it will vigorously pursue such appropriate entities for the collection of their portion of penalty costs pursuant to the applicable terms of the then-current tariff, but if it is unable to collect from such entities, it will seek to treat the uncollectible penalty as it would any other bad debt. As we stressed in the Guidance Order, it is important for RTOs and ISOs to include provisions regarding the appropriate responsibility for reliability-related monetary penalties in their contracts with their members and customers and/or in their tariffs, including provisions regarding the appropriate responsibility for such penalties on the ISOs and RTOs.³² In addition, the Guidance Order states that the Commission will nevertheless entertain section 205 filings by the RTOs and ISOs requesting recovery of penalty costs by spreading those costs among their members and/or customers. However, as the Guidance Order notes, the Commission will consider several factors in its decision to allow recovery of penalties from customers and/or members, including the fairness of

³¹ Schedule 34, section 2(1)(b), Original Sheet No. 2280U.

³² Guidance Order, 122 FERC ¶ 61,247 at P 24. The Guidance Order also noted that "it is the responsibility of registered entities in general, and certainly RTO/ISOs as registered entities, to comply with Reliability Standards for which they are registered and to ensure, contractually or otherwise, that other entities that may be partly or wholly responsible for such compliance will perform in compliance with the applicable Reliability Standards." *Id.* n. 40.

the assessment mechanism proposed by the RTO or ISO.³³ The section 205 proceeding would allow, on a case-by-case basis, the opportunity for parties to argue for or against the allocation of penalty-related costs associated with former Members and/or Tariff Customers, and it would allow new Members and/or Tariff Customers the opportunity to argue for or against the allocation of penalty-related costs incurred before becoming a Midwest ISO Member and/or Tariff Customer. Accordingly, in the event that Midwest ISO makes a section 205 filing with respect to the recovery of penalties, we intend to review any such filing in accordance with the guidelines set forth in the Guidance Order.

41. Finally, we agree that Midwest ISO TOs' proposed changes to section 3 of Schedule 34 make that section more consistent with language included in section 2 and direct Midwest ISO to make a compliance filing to make those changes. First, the addition of "/or" to Original Sheet No. 2280W provides flexibility in the cost allocation methodology to be proposed by Midwest ISO in a section 205 filing, as each situation may dictate a different cost allocation result. Second, the addition of "by NERC, a Regional Entity or the Commission" to the two sentences on Original Sheet No. 2280W clarify the origin of the penalty costs to be allocated pursuant to Schedule 34.

42. Midwest ISO's proposed Schedule 34 and other related tariff changes, with the modifications discussed above, comply with the directives of the Commission's Guidance Order and provide a just and reasonable mechanism for the recovery of the cost of monetary penalties assessed against Midwest ISO for Reliability Standards violations. We will direct Midwest ISO to submit a compliance filing, within thirty days of the date of this order, incorporating the changes directed above.

The Commission orders:

(A) Midwest ISO's filing is hereby conditionally accepted, effective September 9, 2009, as requested, as discussed in the body of this order.

(B) Midwest ISO is hereby directed to submit a compliance filing within 30 days of the date of this order, as discussed in the body of this order.

By the Commission.

(S E A L)

Nathaniel J. Davis, Sr.,
Deputy Secretary.

³³ *Id.* P 27.